

Slide 1 - Logo

Good morning , Commissioners, ladies and gentlemen.

I sincerely value the opportunity to address the conference today. Thank you.

I am here because I believe firmly that the conference needs some balance to the huge weight of evidence produced by the applicants and the economic theory espoused and argued over the past four days.

While I very much respect the calibre and quality of the experts appearing for both applicants and opponents, experience has taught me to maintain a healthy disrespect of academic and economic theory versus what happens in practice.

Experience has also taught me not to believe everything I am told. The applicants are past masters of spin and I believe that without scrutiny such as provided by the Commerce Commission and ACCC processes the alliance could easily be sold as a great idea, which of course it is if you are the airline owners, or managers on incentives.

The applications could be believable if one did not adopt a more sceptical attitude. Indeed certain parts of the theory and evidence produced during this process remind me very much of Hans Christian Andersen's fairytale "The Emperor's New Clothes".

Perhaps in presenting today I am acting the part of the small child, stating the obvious, but in doing so exposing these applications for what they are - a blatant attempt to monopolise and manipulate the New Zealand travel market.

The applicants in their cross submission dated 18 July said...

"Third parties have provided very little in the way of supporting evidence for the statements and assertions made in their submissions. The applicants believe the Commission must prefer the Applicants' submissions, which are backed by substantial and detailed evidence, to the submissions of third parties that are largely unsupported by any objectively verifiable evidence."

This cross submission concluded with point 65.

"The applicants note that none of these third party submitters have demonstrated any special skill or knowledge relative to the statements and assertions that they make."

Unlike many of their hired guns I have not included a verbose CV in my submissions but for the benefit of those assembled here today perhaps I should quickly run through my background.

Slide 2 – CV1

My name is Gerard Murphy. I the owner of a travel agency in Pakuranga, Auckland - Bon Voyage Cruises and Travel. We have a substantial website and growing online business, through e-travel.co.nz.

I have spent seven years in tertiary study part time and hold an NZIM Management Diploma, a graduate diploma in business - with a marketing major and a Masters of Business Administration from the University of Auckland. In addition I hold both Preliminary and Advanced IATA/UFTAA diplomas. I believe therefore that I have an academic and technical background to make a valuable input to this process.

Slide 3 – CV2

My travel experience includes wholesale and retail roles, from consultant to branch management and ownership, and senior marketing management roles for two substantial travel agency chains. Most importantly I have had over 23 years experience in direct and close contact with both travellers and industry suppliers and airlines, including the two applicants. I believe also this gives me the professional industry experience to make a valuable input.

Assertions and statements contained in my two submissions, the cross submission and today's presentation are based on these 23 years of experience and current coal-face participation in the travel market, that the proposed alliance would change substantially, not just for me as a participant but also for the consumers – the travelling public.

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The applicants also criticised the opponents for repetition. Having read countless pages of submissions from the applicants and their experts I need to suggest that this criticism is certainly one of the pot calling the kettle black!

Today I wish to question the quality and accuracy of submissions provided by the applicant's experts. It seems the applicants view is that if they can get enough high powered experts espousing theory, facts and figures that we will all blindly believe them just like in the fairy tale!

The July 28 report of Dr Willig and Margaret Guerin-Calvert is an example. Much of its 52 pages is repeated evidence from other applicant submissions. Further the 12 pages in this report devoted to savings from online fares are completely misleading. Frankly I was shocked at the faulty analysis.

The authors attempt to suggest that the alliance will produce consumer benefits of between \$42M and \$66M. This is based on consumers being able to buy one "online" fare ticket with Air NZ and Qantas between a large number of city pairs beyond the main Trans-Tasman gateways in NZ or Australia, rather than buying, two or more tickets to get to more distant points.

Slide 5 – Fares Table

The authors conveniently overlook the fact that these online/interline fares already exist between Air NZ and Qantas. They cite 20 routing examples to demonstrate savings of an average of 21.1%.

What they fail to tell us is that Air New Zealand currently offers interline through fares at these levels, between at least 414 city pairs combining Air NZ and Qantas flights. Therefore these savings of \$23M to New Zealanders are simply non-existent!

Had the authors consulted a travel agent instead of doing their research over the internet they would have been advised correctly.

Slide 6 – City Pair Points

Even with Air New Zealand's new lower Express Class fares released last week interline through fares are available combining the two carriers. Sure you can't get one ticket from Westport to Wagga Wagga, or Napier to Narrabri, but there are over 400 other combinations. The number of travellers wanting other city pair combinations would be below the margin of error in any statistical analysis.

The applicants may argue that if the Alliance is not approved that Air NZ and Qantas will refuse to co-operate on such fares. This could be true, but is unlikely. Both airlines negotiate with countless other airlines worldwide including competitors to create interline fares in all continents.

Should they in fact refuse to co-operate in this way Qantas themselves would still offer 57 city pairs, and assuming that under the counterfactual Qantas would in fact strengthen its relationship with Origin Pacific, combined they could offer 228 city pairs.

Air New Zealand themselves would offer 115 city pairs, and Virgin Blue could offer between 57 and 95, (depending on whether they have 3, 4 or 5 cities in New Zealand). It needs to be remembered that with VBA entry a combination of two tickets may in fact be considerably cheaper than one ticket online or interline fares anyway!

To summarise - As there will be a huge number of city pair options for one ticket online or interline fares, under the factual and the counterfactual, the claimed savings are simply non-existent!

Slide 7 – 5th Freedom Competition

The analysis of 5th Freedom Competition and Virgin Blue's likely Trans-Tasman entry glosses over some key issues that we raised before:

The 5th Freedom competition is confined to the Auckland market - no-one south of the Bombay Hills benefits directly and there is no real evidence that any 5th freedom carrier will fly south.

The applicants repeat their claim that a number of 5th freedom carriers could commence Trans-Tasman flights just because they a) have rights or b) because they aircraft idle in Australia.

To suggest that United Airlines which terminated services and laid off all NZ staff this year, or American Airlines who have entered and withdrawn from New Zealand twice already, or even that B.A. who are currently suggesting a possible withdrawal from Australia, would re-commence Trans-Tasman operations is a bizarre notion.

Theory would suggest that travellers will be attracted by cheaper fares on 5th Freedom carriers. In practice we find that flight schedules are more important than you may expect. Many leisure travellers are put off by early morning departures from Australia and revert to Air NZ or Qantas paying more in most cases.

Business travellers are attracted by a 5th freedom carriers fares, currently offering savings of close to \$900 in economy class for a mid-week business trip. But they are put off by having to purchase additional accommodation to make their itinerary work and in most cases losing a day due to schedules, even though the saving could still be \$300-\$500. I had an example of this just yesterday.

Slide 8 – Virgin Blue

The applicants suggest that Virgin Blue's recent Boeing order means that Virgin will be able to allocate resources here at the drop of a hat. Virgin's early publicity suggested that six Boeing 737s would be allocated to off-shore routes from Australia, including Fiji, Vanuatu and NZ, in the short term.

Even if Virgin did allocate all six aircraft to New Zealand it would not be enough to provide credible competition to the Alliance Trans-Tasman, particularly if they are expected to run up and down the main trunk with the same fleet.

David Huttner's suggestion last week that a market share closer to 30% was required to provide truly effective competition, seems to have been confirmed by Geoff Dixon's announcement that 30% was the line in the sand that Qantas would vigorously defend.

Slide 9 – Virgin Blue – TT Seat shares

In the short to medium term an Alliance would still be able to dominate, particularly south of the Bombay Hills, - the 2/3 of New Zealand seemingly ignored by the applicants in this process. I have added a possible Virgin Blue schedule (using 5 x 737 aircraft) to table 3 from Dr Willig's report. The resulting table shows that apart from Auckland to Brisbane and Melbourne, Qantas and Air New Zealand would still have significant shares or dominate most routes, and they could correct any loss of share simply by adding slightly to their schedules.

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There have been a number of comments that Virgin would look at operating to/from any centre with a population of 50,000 or more. I suggest this figure is off the mark.

I have looked at Southwest, JetBlue, Sky West, and indeed Virgin Blue and found that apart from a handful of ports most of their destinations have populations much closer to 100,000 often many more. I would suggest that the minimum economic population base for a 737 service is more like 100,000.

A tourist destination with a lower population can also be successful and explains Virgin Blue's services to Broome and Whitsundays. Most of Virgin Blue's routes have a city of 1 million plus at one end of the sector. So as recognised by Dr Willig a 50,000 population is only part of the equation.

Given population catchments, distance from existing VBA ports and current airport infrastructure I would suggest only Napier, Rotorua, and Nelson/Blenheim would be considered as new VBA ports. Access to these ports would depend on council and/or investor initiative to upgrade and/or extend runways and airport facilities.

The facts are that if Virgin Blue does decide to operate domestically in New Zealand it is currently limited by 737 capable airports meaning it could only fly the main trunk including Dunedin, plus Queenstown, Hamilton and Palmerston North until new airport facilities are available. This means that Virgin Blue will not provide true competition to Air NZ's very effective domestic network.

Recognising this, the applicant's Ivy League experts have conveniently paired off Virgin Blue with Qantas' discarded friend, Origin Pacific. They assume the two could cobble together a worthwhile working relationship and provide some competition to their monopoly. This is an arranged marriage without the bride and groom even having the opportunity to court!

Air New Zealand has a dominant share of the NZ domestic market because of its network combining main trunk jet services and its comprehensive provincial route structure.

Currently Qantas loses substantial business, as would Virgin or Origin Pacific individually or together, as they cannot provide the same 'seamless' service and network connections. Connecting and open-jaw passengers are constantly forced back on to Air NZ.

Regardless of Air NZ's move to switch customers to online/internet reservations approx 60% of all domestic travel is still transacted by travel agents. Unless Virgin and Origin can truly work in partnership, co-ordinating schedules and sharing common reservation systems accessible to travel agents there will be no true competition on domestic New Zealand routes.

FARE INCREASES & UNDERTAKINGS

The probability of the merged applicants using their market position to manipulate the market and raise prices has been raised in a number of submissions. The applicants through their experts have produced evidence in an attempt to dispel these beliefs.

The applicants have offered several undertakings including an offer to maintain airfares at current levels. In an earlier submission we demonstrated how an airline could maintain an advertised low fare, yet manipulate its seat stock using sophisticated yield management systems to achieve real fare increases.

The introduction of Trans-Tasman Express Class last week gives us some indication of the airlines real intentions with fare structures. The airline's own literature states that they would offer 25% on average of its seats at the lower level "Smart Fares".

Slide 11 – Air NZ Express Fares

Of course the flip side of this statement is that 75% of its seats will be sold at higher levels, "Flexi Saver Fares" or "Flexi" fares . These fares start at \$589.00 and if booked by phone or in person cost \$50 more, making a total of \$639.00. Hardly any saving really on the pre-Express fare levels.

The Express Fare introduction gives a very real example of the airline's ability to use its position, and more 'covert' methods to increase fares in real terms. Currently larger corporate clients will generally have a contract with Air New Zealand (and or Qantas) offering Trans-Tasman fares with relaxed conditions eg no Saturday night requirement, refund ability and ticket change flexibility. These fares may be anywhere from \$600-800 depending on client company size.

Slide 12 – Air NZ Express - Corporate

With the introduction of Express Class Air New Zealand has announced that these fare contracts will not be renewed. Under the new fare structure a fare to offering similar flexibility will be starting at \$1078.00, a huge increase! While we accept that companies could take the cheapest Express fares our experience with the same fare structure on domestic routes is that clients are forced to buy the flexible fare levels, as the risks of lower 'use it or lose it' fares are just too great.

This is a demonstration of the fare increase mechanisms available to the airlines. If the application is approved I am sure that these fare increases to major corporates will proceed. Under the counterfactual Qantas may have other ideas and compete for this business on price, forcing Air New Zealand to back down. Unfortunately no other carrier has the route network, or frequency to compete for this high volume corporate business.

Slide 13 - Loyalty Schemes

We agree with the Commerce Commission that lack of loyalty schemes could be an issue for a new entrant.

We note in the Willig/Guerin-Calvert report that the applicants claim that 21 and 29% of their Trans-Tasman travellers were frequent flyer scheme members. These figures are surprisingly low and are vastly different to our experience. A quick poll of our current bookings shows that 83% of international longhaul passengers and 64% of Trans-Tasman passengers will be affiliated frequent flyer members of the airline they are flying.

The status level of the members is irrelevant. The applicants and credit card companies have encouraged millions of people to join frequent flyer schemes, and each traveller member believes he or she will benefit. Indeed a member does not have to have an "elevated" status i.e. they actually fly frequently, as suggested by the Willig report to enjoy reward travel. A return trip to London plus one trans-Tasman flight will give members of most schemes a further Trans-Tasman trip, but still not offer them an elevated status.

While a new airline, such as Virgin Blue, can enter the market without a scheme, if fares are competitive a frequent flyer member will always choose his usual airline. As many will be aware consumer behaviour is not always rational. On many occasions we have had people choose 'their' airline to earn points, paying a 'surcharge' to do so. Often the additional fare costs far outweigh the benefit that the earned points will bring.

Qantas and Air New Zealand have over 3 million members in their schemes. This database can be used as a weapon of mass reservation in the battle of the Tasman - that is a distinct competitive advantage to the alliance.

A number of VBA's do have Frequent Flyer Schemes. Southwest have "Rapid Rewards" , JetBlue have "TrueBlue", and WestJet offer "Air Miles". It is rumoured in Australia that Virgin Blue is also soon to release its own frequent flyer scheme, so it seems these leading VBA's see the need for loyalty schemes.

It is interesting that our applicants want us to believe it is unimportant – I am sure they would squeal if a condition of the alliance approval was that frequent flyer benefits could not be offered on the Trans-Tasman or domestic markets!

Other Markets:

I am seriously concerned how little focus has been given to other markets that will be seriously affected by the proposed alliance, until last week it seems.

Slide 14 – Departure Stats

In our earlier submissions we identified that the North American Market will be monopolised and a number of other markets will come under the influence of the Alliance and its partner or code-carriers. These markets include Japan, Hong Kong, Fiji, Samoa and New Caledonia.

These routes account for close to 15% of all outbound departures, and 17.3% of all business travel departures from New Zealand, not including travel to Europe via North America.

Slide 15 – Visitor Arrival Stats

The North American routes alone are even more vital to New Zealand's tourism interests producing 12% of all visitor arrivals, and these are the cream of all tourists, again not accounting for travel from Europe via North America.

The North American routes are clearly extremely important both outbound and inbound, and it is equally clear that the Alliance will have an absolute monopoly on these routes. For this reason alone the applications should be rejected.

Please also consider the importance of Japan, and Hong Kong, usually. The relationship that Air New Zealand and Qantas have with Japan Airlines, and Qantas has with Cathay Pacific means that coupled with the other routes, they will have virtual control of more than 35%* (**should have read "control of 22%"**) of our inbound tourist arrivals, on top of the huge influence they will exert over the tourist market from Australia, which alone accounts for nearly 50%* (**should have read 31%**) of our tourist arrivals. * stated figures were incorrect due excel error – corrected figures are show in brackets.

Having one airline group with control or serious influence over such a huge proportion of our inbound market is simply unacceptable.

Oneworld and Star Alliance

Finally I would like to look at the Oneworld and Star Alliance Relationships. The power of these relationships can not be underestimated, and I believe it is of vital importance for New Zealand to have strong members of each flying into New Zealand.

With the merger it is highly likely Air New Zealand will be forced to leave the Star Alliance. This means that there will be no Star Alliance carrier operating between here and North America, Japan or Hong Kong! This will seriously compromise access to New Zealand for millions of potential tourists on round the world type tickets.

United Airlines and Lufthansa alone have close to 50 million frequent flyer members who will likely no longer consider New Zealand in their holiday decisions. Anecdotal evidence said that United Airlines load factors were considerably enhanced by their frequent flyers using points tickets. These tourists simply won't come if Air NZ is unavailable to them!

In addition many thousands of New Zealand travellers who currently enjoy the benefits of Star Alliance fares and Star Alliance loyalty programmes will simply have these benefits taken from them.

Conclusion : I believe the benefits of the Qantas / Air New Zealand Alliance have been seriously overstated and the downside seriously understated by the applicants.

Air New Zealand is not in dire straights, as will be proven this week. There will not be a war of attrition; it is in no-one's interest. Indeed Dr Willig states in point 60 of the 28 July report that, "if an incumbent does not believe that it can force the entrant out of the market, it will not have the incentive to engage in predatory behaviour" I think this statement applies as much to competitors as new entrants.

I hope that the Commission has seen comprehensive evidence that Air New Zealand has actually seriously examined other strategic options other than the Qantas merger. I doubt any alternative has seriously been pursued. Indeed Mr Norris' opening remarks implied management had considered just two but only briefly, and only because the board required them too. It seems they have their heart set on just one outcome! One hopes however, that somewhere there is a Plan B, as I am sure Qantas have a B and probably a C, or D.

In the interests of New Zealand, our travellers and visitors I believe it is vital that we maintain Air New Zealand as an independent entity, competing against Qantas and all comers. New Zealanders use initiative, innovate and find Plan B's. We go around obstacles, not wait for them to crush us.

To say that Air New Zealand will fail without this alliance is simply one horrific ending to this story. But as we all know fairy tales usually have a happy ending!

Has Air New Zealand met the beautiful princess? Is her name Qantas? I think not. She may be a witch in disguise! Luckily the wise people at the commission can save him, and he can go searching in far off lands for the beautiful princess.

Could this princess too be from the land of alliances? Could her name be Star? Will they marry and everybody live happily ever after? The future was left in the hands of the wise commissioners, and all the people of the land wished them well!

The end!